# A STUDY ON MUNICIPAL PROPERTY TAX STRUCTURE AND TRENDS IN SELECTED CITIES OF INDIA

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## Introduction

Cities in India are constrained by limited municipal revenues and resources to undertake necessary public investments for providing urban infrastructure and services on a sustainable basis. This comes in the way of harnessing their potential as critical drivers of economic growth and development, despite the 74th Constitutional Amendment Act, 1992 for statutory provision for urban administration and subsequent reform measures introduced to empower cities. The problem of municipal revenue deficit can be addressed through two steps: (a) increasing revenue from existing local taxes, and (b) strengthening the revenue-raising power of the city-level municipal governments or urban local bodies (ULBs) by broadening the sources of revenue base.

Property taxes are widely regarded as an efficient and equitable means of raising revenue, but with a revenue potential that is largely untapped in many countries. Property taxes generally yield relatively modest revenue, particularly in developing and emerging economies, but there are also large disparities across countries which signal popular opposition as well as technical constraints in their administration—but also a potential for enhanced utilization. The differences of opinion are probably starker on property taxation than on most other taxes. While economists tend to strongly favour increased reliance on property taxes owing to their attractive economic properties, there is a widespread popular and hence political resistance to their increased use stemming in part from their transparency and relatively limited scope for tax avoidance and evasion.

## The Concept and Relevance of Property Tax for Municipal Governments

The property tax refers to the taxes imposed on the holding of property, including both residential property and business property. A property tax system involves six major functions: tax base identification; tax base valuation; tax assessment; tax collection; tax enforcement; and dispute resolution and taxpayer service **(Kelly 2000).** Each of these functions is linked to four critical ratios of coverage, valuation, tax, and collection. The conceptual model of property tax revenue illustrates the relationship between total revenue collection and these various ratios. Hence it is not an easy-administered tax.

From a legal point of view, property tax is nominally paid by the owner the household. For administrative convenience, the renter or user of the real estate may also share the responsibility to pay the tax. However, from the economic point view, the person who ultimately burdens the tax may not always be the people that pay the tax. Tax liability can shift forward or backward the market system.

Theory and international best practices identify that property taxes on land and improvements are the ideal tax for funding local government level services for a number of reasons:

Firstly, property-related taxes have a strong potential for revenue mobilization, especially in rapidly urbanizing areas. In fact, urbanization is a wealth-creating process, causing rising land values, which, if appropriately captured, can provide funding for much needed urban infrastructure and services.

Secondly, the property tax base is immobile, which minimizes economic efficiency implications and is considered the least distortive tax instrument followed by consumption taxes, personal income taxes and corporate income taxes, respectively (Johansson, Heady, Arnold, Brys and Vertia 2008). Due to its immobility, the property tax base captures the value of location-specific capital investments and benefits from government programs and services not captured otherwise through various fees, user charges, and other taxes. This allows the property tax to operate as a form of "benefits tax," allocating the tax burden across properties with differential benefits as reflected in differential property values. The immovable property tax base also makes it relatively easier to identify and capture the tax base and allows the property itself to be natural collateral in case of tax non-payment. *f* The property tax base also tends to fall more on those with the "ability to pay," as immovable property is often a primary repository of wealth.

Finally, as a highly visible and politically sensitive revenue instrument, the property tax base can encourage more responsive, efficient, and accountable local governance and public service delivery. Recurrent property taxes are justified primarily as "benefit taxes" or as "quasi-user charges" for local public services received. This "benefit principle" in public finance argues that the tax/charge amount should be paid by those benefitting from government-provided services. For many government services (such as water supply, public transportation such as buses, and solid waste collection), it is technically possible to use a set of direct user charges linked to the benefits that can offset the costs of those public services. When people perceive this connection between taxation and services, they are typically more willing to pay their property taxes. Those public service benefits not properly charged and captured through user charges are often reflected ("capitalized") in property values. Thus,

public infrastructure improvements and other public services (such as location-specific social services), are typically captured in increased property values as residents are willing to pay higher property prices for properties with improved accessibility, drainage, school options, medical facilities, street lights, and security, among others. Thus, there is a connection between local, location-related services, and property values—which is why property taxes are typically assessed on an ad valorem or value basis. When people perceive this connection between taxation and services, they are typically more willing to pay their property taxes. In one sense, the property tax can be seen as simply a payment for local level public services, similar to purchases of goods and services within private markets, thus helping to improve the efficiency link between the costs and benefits of public services. In addition, the property tax is an excellent tax to improve the governance "accountability" linkage between local-level governments and their local residents. Despite its many benefits, it is worth noting that the property tax tends to be a politically sensitive tax. As a direct tax, it is visible; tax payments can be quite "lumpy" and often bear little direct relationship to public service delivery.

The importance of the municipal property tax as a source of financing tends to be overlooked because fiscal analysis normally focuses on central government or state finances, and in that context the property tax is a relatively minor source of revenue **(McCluskey,1998**). Despite the relatively low contribution of property taxes to national revenue, virtually all countries seem to be focusing on strengthening the property tax, the most common revenue source for local governments throughout the world **(Kelly, 2000).** One reason that taxes on land and property have been considered to be especially appropriate as a local revenue source is that real property is immovable-it is unable to shift location in response to the tax and is the connection between many of the services typically funded at the local level and the benefit to property values **(Bird and Slack 2002).**

In India, Property Tax is levied by the municipal authorities on real estate. It is based on the value of the property and the rate of property tax and manner of valuation varies from one municipal authority to the other. Property Tax, also sometimes known as House Tax, is the tax imposed on real estate owners by the municipal authorities like panchayat, municipality or municipal corporation which is used for maintenance and upkeep of the local civic amenities of the area, like roads, sewage system, lighting, parks, and other infrastructure facilities. It is usually levied on all real estate, including buildings (residential or commercial), attached land, and improvements made to the land, but not on vacant plots of land with no adjoining building.

**Municipal Property Tax Structure in India**

In Indian federation, the Seventh Schedule of the Constitution assigns the legislative powers of the Union and State governments. Entry 4 in the state list empowers the state governments in all matters relating to local governments, including "...the constitution of powers of municipal corporations, improvement trusts, district boards, mining settlement authorities, and other local authorities for the purpose of local self-government or village administration". Under Article 243-W, the legislature of a State, at its discretion, is authorised to devolve powers to the municipal governments on functions listed in Schedule 12 of the Constitution. Similarly, Article 243-X authorises the State governments to devolve the power to levy taxes, duties, fees, tolls according to the limits set and procedure laid down by the legislature of the State government. The above assignment system has entailed three important features.

First, while there is a separate schedule indicated for the devolution of functions of municipal governments, though the specific function to be devolved and the extent of devolution lies with the state government, there is no separate list of taxes indicated in the Constitution for assignment to the municipal governments. As there is no separate list for local governments, the State governments are required to assign the tax powers to local governments from the State List in the Seventh Schedule.

Second, the assignment of functions and sources of finance to municipal bodies is to be done at the complete discretion of State governments.

Finally, the local governments are given the power to levy taxes, duties, fees and tolls in accordance with the procedures and limits specified the State governments. Entry 49 empowers the State governments to levy 'taxes on land and buildings 'which has been devolved to the local governments. However, in the statues governing the municipal governments, the State governments lay down the procedures for valuation, exemptions and concessions, the floor and ceiling rates of tax and administrative and enforcement mechanisms on matters such as delays, arrears, and evasion. Thus, although taxes on immovable properties are considered to be a local levy, local governments have very limited autonomy in determining the base, fixing the rates and enforcing the tax.

Municipal Property Tax is an important source of local revenue in many countries **(Lall and Deichmann 2006).** But urban Property Tax levied by municipalities is an underused source of revenue in India **(ibid.).** It has also been argued that the weakness of Municipal Property Tax is perhaps best exemplified by India **(Davey and Devas 1996).** It has been argued that Municipal Tax is based on 'benefit principle' as against Wealth and Inheritance

Taxes, which are based on the 'ability to pay principle' **(Mathur et al 2009).** Therefore, Municipal Tax is not for distributive justice but for municipal services **(Mathur et al 2009, Government of India 2009)** and self -financing of urban development. Apart from rates that are low relative to the cost of municipal services, setting the tax base is challenging because of the absence of a reliable count of properties. Collection efficiency is low, with only 63 percent of assessed properties actually paying taxes in the "large city sample", and it is estimated that this amount to 56 percent of the universe of properties. Even for the house properties actually assessed, poor collection efficiency, at 37 percent of demand for the sample, along with the non-indexation of property values have exacerbated the problem **(Government of India 2009).**

Urban areas generate about 65 per cent of the GDP in the country. The Indian government (Centre and States combined), which spends only around 6.7 percent of GDP on its social sectors (such as education, health, water and sanitation) compared to 14 percent of GDP for OECD countries on average (**CBGA 2012),** can gain considerably from a progressive Property Tax. Unfortunately, reliable data on revenue collections from property tax by various municipal bodies is not available in India. Both the 13$^{th}$ Finance Commission and the HPEC, in their reports, have used the estimates made by **Mathuret. al (2008)** which has questions of reliability.

Very few municipal governments in the world update the property values for taxation purposes every year (**Slack, 2011).** The simple fact is that whoever is the base taken –the annual letting value, capital value or an area-based value, the value finally taken as the base is presumptive. Given that a 'representative' value has to be taken for each locality, the value chosen will be the minimum rather than average. In other words, any presumptive value of the tax base will be accepted only when this is substantially lower than the actual value of the properties. Furthermore, increases in the market values for the property owners is only an accrual and will not be realized unless they sell their properties and therefore, it will be difficult to include higher value of the property that has accrued and not realized in the tax base. Not surprisingly, even as the immovable property values in urban areas have been increasing at a rate much faster than general inflation rate and even as there has been significant increase in the number of houses in urban areas, the revenue productivity of property tax has continued to be low.

**Municipal Property Tax Variations across Cities in India**

The economic rationale for property tax is that it enables urban local bodies to capture a part of the "unearned" increase in property values. The urban property values rise as a result of infrastructure investments by urban local bodies (e.g., a road facing property or a park facing property has higher value than nearby properties in the same location). It is also a "progressive" tax, as higher value properties pay higher taxes. The economic rationale for property tax is that it enables urban local bodies to capture a part of the "unearned" increase in property values.

Property tax revenue as a share of GDP in India was 0.15 % in 2017-'18, which compares unfavourably with 0.6 % for developing countries and 2.1 % for developed countries. It also suggests a potential to increase property tax revenues at least four to five times when compared with developing countries. On average, only 37% of the tax demanded is collected, with the corresponding figures being as low as 55% for a city like Mumbai (Collier et al. 2018, Chattopadhyay 2015). In spite of the penal provision for delayed payments or non-payments, ULBs rarely undertake any penal action against the defaulters, highlighting the role of local political economy, and lackadaisical nature of commitment. Further, exempted properties in India constitute approximately 10% of the total urban properties, and about 11% of the assessed properties.

Property tax revenue accounted for 0.15 percent share of the Gross Domestic Product (GDP). Cities across India are in the quandary over poor tax collections till now, and the possibility of the pandemic condition deteriorating it further. On 14 September 2020, the Bangalore civic body declared that it had collected property tax of Rs 19,160 million as opposed to over Rs 20,000 million in 2019. A similar trend was seen with the Ahmedabad Municipal Corporation which collected Rs 6,020 million till August in 2019, has managed to collect Rs 5,050 million between 1 April and 28 August this year. This has come after the corporation extended a 10 percent rebate scheme by 31 August, 2020 for early tax payers. The Mumbai civic body, on the other hand, hasn't been able to get any revenue from property tax in its kitty because of a pending decision of waiving off taxes for all properties under 500 square feet in the city. Propertytax accounts for 24 percent of the Mumbai city revenue and this decision is likely to set it back by over Rs 3,000 million.

**Municipal Property Tax Valuation Methods in Indian Cities**

- Annual rateable value (ARV) with rent as the basis (hypothetical rent)
- Annual rateable value (ARV) with unit area characteristics representing the base

- Capital valuation
- Tax rate applied directly to carpe

The valuation systems are to be so designed as to capture the market value of properties. Market value is determined on the one hand, by demand and supply factors, and on the other hand, specific location factors, which include the quality of municipal services. It is hypothesized, that market value is best reflected in the sale value of a property which, in combination with other factors, is determined by the capitalised value of services provided by municipal bodies, a part of which the municipalities recover via taxation of properties. Thus, "rents" and the extent to which they determine the ARV and the capital values wherever the sale value of properties is used, represent the market conditions and are considered to be an indicator of market valuation. In one way or the other, "market conditions" are implicit in other methods of valuation as well. In India, none of the methods outlined above approximate the market value of properties. For example, instead of the actual rents, hypothetical rents are used for determining the ARVs. Guidance values form the base for determining the market value of properties instead of the actual sale and purchase values. Guidance values represent anywhere between 20-40 percent of the market value of properties. Unit area values are also adjusted, ostensibly on the ground that the market value of properties as the tax base would place a disproportionately large burden on property tax payers.

Along with the fair valuation of property, periodic and regular re-assessment of the property tax base is critical to bring assessed values in line with market realities. In municipal Acts of many states, it is recommended to carry out an assessment of properties once in every five or four years.When such assessments are done only every four or five years the sudden increase in tax payable in the year of re-assessment leads to a drop in collection efficiency. This could be overcome if the tax rates are increased every year as gradual increases are likely to be more acceptable to property owners.

Two distinct assessment methodologies, as practiced in Indian cities, value-based assessment and area-based assessment[1] (with the former being divided into rental[2] and capital value[3] approaches) have failed to capture the real value of properties. Non-availability of extensive data on market transactions of properties (or the corresponding from revenue departments) makes the valuation under capital value approach inaccurate. Assessment of rental value based on current use (actual rents paid) rather than the highest and best use coupled with wide use of rent controls also reduces the efficacy of the rental value approaches. Cities like Bangalore, Chennai, Hyderabad, Indore, Kolkata, Patna, and Pune

have introduced Self-Assessment System (SAS) as a reform measure. In this system, the rental values of the properties are determined based on the property information provided by the owners themselves. Self-assessment is genuinely an appealing procedure for Indian cities with little administrative capacity. However, possibility of underestimation with generally lesser incidence of the same among the lower-valued properties compared to the higher-valued properties could produce significant revenue losses. Fair initial assessment and periodic re-evaluation of properties reflecting changes in value could be useful for addressing inelasticity in the Property tax (PT)

Regarding the rate of PT, most ULBs have followed a progressive rate structure. In contrast, Bangalore and Ludhiana have tried a flat tax rate, where rates are different for residential and non-residential units, and they are lower for owner-occupied as compared to rented houses. Area-based system of assessment is very simple as it is based on covered area of building, and unit area value or tax for the category in which the property is located.Under rental value approach, property is assessed according to estimated rental value or net rent.Capital value approach assesses properties on the basis of their market value

**Municipal Property Tax Reforms- Need for strategising the reforms**

The Ministry of Finance, as part of the additional borrowing of 2% of Gross State Domestic Product to states for 2020-'21 under the Atmanirbhar Bharat Abhiyan, has called for states to reform property tax valuation, by linking floor rates to prevailing guidance values/circle rates and putting in a system for periodic revision of property tax rates in line with an increase in price. The Ministry of Housing and Urban Affairs has recently issued a toolkit for property tax reforms to help states and local governments meet these conditionalities.

It is not for the first time that the government of India has attempted to reform property tax. Reforms were initiated under the Jawaharlal Nehru National Urban Renewal Mission. It required states/ cities to undertake reforms in property taxes, with the objective of "establishing a simple, transparent, nondiscretionary and equitable property tax regime that encourages voluntary compliance". These reforms have continued under the Atal Mission for Rejuvenation and Urban Transformation. Thus, for the past 15 years, property tax reforms have been linked to financial incentives from the centrally sponsored programmes. Despite this, the need to include property tax reforms by Fifteenth Finance Commission and the Atamanirbhar Bharat Abhiyan may suggest that the previous reforms did not yield adequate results.

Apart from improving the valuation or expanding the tax base, efficient and effective tax collection and management are essential to strategise the PT reform. Complete digitisation of property records, usage of insights from the evidence generated, billing and payment system including introduction of new modes of tax payments could surely improve the efficiency in tax collection. Increasing tax compliance also requires identification of tax defaulters and initiation of penal actions against them regularly.

Effective implementation of measures like imposition of fine as a percentage of the tax due, publication of defaulters' lists, combining tax liabilities with utility payments, prohibiting sale of properties or withholding permission of development without up-to-date tax payment, providing discounts to the taxpayers for timely payments of PT, and so on, are likely to enhance tax compliance. It is also important to sensitise people about PT payments by showcasing the various costs and benefits of compliance and/or non-compliance to tax regime. Government of India's push on urbanisation, and infusing a spirit of competitiveness among cities through various programmes (Smart Cities Mission, Atal Mission for Rejuvenation and Urban Transformation, Heritage City Development and Augmentation Yojana), rankings (SwacchSurvekshan, Ease of Living Index, etc.) and ratings (credit ratings of ULBs, other performance standards), should also prioritise the empowerment of ULBs. Focus should be on their capacity development, and on enhancing their performance to harness the potential of PT as one of their primary sources of revenue.

Despite all the reforms, it is important that we consider that property tax cannot be an end in itself for solving the issue of insufficient funds in cities. Property tax has remained stagnant for years and the government needs to help cities, which are highly-dependent on state and central transfers, to become independent. Several taxes like octroi, advertisement tax, local body tax which gave liquidity to ULB's got subsumed within the GST leaving them even more dry. While the government is giving property tax reforms a push it could be enabling to levying betterment and impact fees on land could be considered. Cities need to become financially independent and the property tax reform will be a starting point towards their economic autonomy.

To implement the reforms, it is imperative that all state governments set up the proposed Property Tax Board' on a war-footing and sets stringent rules to reprimand both erring ULB's and tax payers. The board, a concept that has been pushed right from the 13$^{th}$ Finance commission has come into force in a diluted form in states like Tamil Nadu, Andhra Pradesh and Maharashtra. The board which is advisory in nature would look at reviewing property tax

assessment systems, reworking valuation methods, and ensure that collection systems are more technologically upgraded and dynamic. Interestingly,

**Background of the study**

The above introductory analysis forms the study background. Hence it is very clear and understood that Municipal property tax is highly important source of locally raised revenue required for government expenditure in many parts of the country. It makes the reliable internal source revenue for local governments. In a traditional point of view, property tax has been identified with local government for reasons of its visibility and the inability of the tax object to shift location as a result of the imposed tax (**Mosha 2010).** Property tax is considered as relevant local source of revenue because of the linkage between the type of services provided by local government and the enhancement in property values.

Revenue from property tax spent on different services such as fire, police protection, roads, drainage, street lighting results in increased property values within the jurisdiction. It is internally, the increasing demand of public services and the local government need to finance some of its project by revenue from property tax making it an issue of concern globally that decussated many countries to impose tax on real property (Roy, 2009).

The local government is interested on revenue from property taxes to finance local social services provision to the people. Property tax has an opportunity to enhance public fiscal policy decision on local government expenditure therefore is required by the local Government **(Bird, 2001).**In developing countries property tax is an issue of concern that has potential effect on local government revenue required for public finance. Property taxes bring diversity and help to balance the state and local revenue system. Property tax on the current market value is an important part of property taxation system because a market value-based property tax has a comparatively stable and reliable base that is attractive during troubled economic (**Franzsen&Semboja, 2004).** Property tax is very special ingredient of fiscal policy for municipal governments and the most important required local government source of revenue in most countries.

**Significance of the study and Statement of the problem**

Local bodies in India have been conceived as institutions of self-governance which would be prime instruments of decentralization. The success of these organizations depends largely on their financial resources. The acceptance of decentralized administrative system giving more powers and responsibilities to the local bodies resulted in the expansion of the scope of local government expenditure. They must be able to produce their own resources to perform the functions of regulatory and development. Property taxes stood as a major source of municipal

revenue in India. The Finance Unit of the Municipal Council is responsible for the management of property taxes for that area. It is assessed for each item found in the limit based on the various methods and the tax rate is determined in each state. The provision of adequate taxation, revenue collection, tax resources for local bodies varies from province to province and from province to council. There is no uniformity in their connection. These problems can be better understood by conducting a comparative study of Municipal Property tax and its progressivity strategies in various selected Indian cities. There is therefore a need to study the importance and problems associated with local tax collection and its development. The current study therefore revealed Municipal Property Tax Structure and trends in Indian cities. Hence the study is an attempt to undertake a study of Municipal Property Tax Structure and Trends in Selected Cities of Indiawith regard to property tax and its progressivity in the selected Indian cities with reference to Mumbai, Bengaluru, Hyderabad, Ahmedabad, Chennai and Kolkata combined in order to suggest the suitable strategies to sustain and/or improve their financial management.

**Objectives of the study**

- To study the nature and structure of municipal property tax base and trends in the major selected cities in India.
- To examine the trends in the progress of municipal property tax revenues and to evaluate the reasons for its slow growth in the selected cities of India.
- To study the existing methods and defects of computing municipal property taxes and to analyse its impacts on municipal tax revenue mobilisation.
- To find out the existing municipal property tax reforms and its implications on municipalrevenue mobilisation and the need for improve the tax administration.at the urban local level.

**Hypotheses of the study**

- The revenue performance of municipal property tax is significantly affected by the methods of valuation and collection rates.
- The Municipal Property tax tends to be inelastic without regular revision of the tax rates and revaluation of bases intervals.
- The property tax is progressive to the extent it is structured, and is regressive as it falls primarily on house owner and commercial activity.
- Absence of the market-based property valuation depress the property values and tax yields.

**Methodology of the study**

This study was based on secondary data. The data has been rigorously analysed and presented in bivariate and multivariate tables. The simple statistical tools simple percentages, Annual Compound Growth Rate (ACGR) and ratios, chi-square test, f-test and Annova test have been carried out to analyse the various financial resources and functional expenditure pattern under various financial reports of selected metro cities in India. Charts and graphical representations have been drawn wherever necessary.

**Study Area and Data support**

For the purpose of fulfilling the objectives and to test the hypotheses as listed above, the study concentrated on generation of information and required data support through by using secondary data. The study area is limited to 6 major cities in India which are Mumbai, which has the largest Municipal Corporation in terms of population governed, collects almost as much property tax as Bengaluru, Hyderabad, Ahmedabad, Chennai and Kolkata combined.

The data have been collected through secondary sources of annual reports of these six municipal corporations, web site of all the municipalities, various finance reports of State governments and local governments and various reports from Brihanmumbai Municipal Corporation (BMC), Bruhat Bengaluru MahanagaraPalike (BBMP), Greater Hyderabad Municipal Corporation (GHMC), Ahmedabad Municipal Corporation (AMC), Greater Chennai Corporation ( GCC), Kolkata Municipal Corporation, websites and past records from various government reports.

**Statistical Tools used for data analysis**

The data collected from secondary sources are suitably classified and analyzed keeping in view the objectives of the study. For the purpose of analysis, the study used simple percentages, Annual Compound Growth Rate (ACGR) and ratios. Besides, the study also used statistical tools such as chi-square test, f-test and ANOVAs test wherever required to test the hypothesis. Charts and graphical representations have been provided to highlight the data in a systematic manner and the results obtained thereby have been interpreted.

**Scope and Limitations of the Study**

Though there is much variation in the importance of the property tax as a local revenue source, it generally is the dominant local government tax. However, the evidence here indicates that the revenue yield performance of property taxes is weak. The absence of reliable data is only one impediment to creating a valuation roll in the growing cities in India. The private ownership of property is limited, and the concept of an arm's-length property market may be completely new. Naturally the question that emerge; can a property tax

succeed in such an environment? Because of data limitations, careful econometric estimation of the income elasticity of the property tax is not possible, but these data do suggest, even if only indirectly, a relatively low-income elasticity of property tax revenues. The relatively low growth in property tax revenues is also due in large to the inability of local government to reassess property so that actual property value growth is matched by growth in the assessed value base.

The study would have better policy outcomes and analyses relating to municipal property taxes as only a few studies are conducted across the country in particular in Karnataka. The policy suggestions that the research findings likely to derive will have definitely useful to the urban local governments as they would be benefited in evolving a broader scope oriented and effective reforms so as to ensure and adopt efficient tax measurement methods and collection efforts for the future. But the limitations in generating both primary and secondary cannot be ruled out as the accessibility and revealing the data by the concerned difficult to expect on time.

**Conclusions**

Consultation and involvement of the public at various stages of planning, design and implementation of property tax reforms is also critical for its success. The willingness of the property owners to pay increased taxes is likely to be higher if they are made aware that their tax rupee is going towards service improvements. For this to happen, there is a need for transparency and greater awareness among the public about the costs of services in their cities.

Thus, the above analysis related to the municipal property taxes reveals that there is the need to carry out further study aiming to adopt very efficient method and mode of urban property valuation and collection methods. There is also the need for improving the structure of the municipal property taxes and efforts to improve its progressivity in the Indian Cities. With this objective the present study proposes to find out the reality of the issue by considering a growing Municipal Corporation Cities in India.

**The chapter scheme of the study is presented as below:**

| CHAPTER DESIGN |
|---|
| **CHAPTER I – INTRODUCTION** |
| Introduction Background of the study-Statement of the problem -Objectives-Hypothesis- Methodology- Study Area and Data support- Statistical tools applied - Scope and limitations of the study-ChapterisationPattern-Conclusion |
| **CHAPTER 2. REVIEW OF LITERATURE** |
| Theoretical Issues in Property Tax Structure Systems in India-Review of Literature-Research gap –Conclusion |
| **CHAPTER 3.THE ANALYSIS OF MUNICIPAL PROPERTY TAX STRUCTUREAND TRENDS IN THE SELECTED CITIES OF INDI**A |
| Types of Property Taxes-Present State of Property Taxes -Classification of Urban Settlements-Requirements for a property tax system- The analysis of Structure and the growth trends in the municipal property tax revenues in the selected cities of India. -Major impediment to raise property tax revenue-conclusion |
| **CHAPTER 4.THEMETHODS OF VALUATION OF MUNICIPAL PROPERTY TAXES AND ITS IMPACTS** |
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| The municipal property tax reforms- the existing municipal property tax reforms and reform measures initiated in selected cities of India and its implications on municipalrevenue mobilisation and the need for improve the tax administration.at the municipal level-Conclusion |
| **CHAPTER 6. - SUMMARY AND CONCLUSION** |
| Summary-Major Findings-Suggestions-Conclusion |

**Municipal Property Tax: Theoretical Issues**

The design and implementation issues relating to property tax is one of the relatively less researched areas. This is particularly so in developing countries where the property market is largely unorganized and therefore, valuations are extremely difficult, information available to the tax authorities is restricted, extent of decentralization is limited, the local elite or "distributional coalitions" are powerful and there are serious capacity limitations for the levy designing and implementing the property tax. In fact, in most of the developing countries, the vicious cycle of low service quality, low tax compliance leading to further low level of local public services continues to persist. While it is acknowledged that the metropolitan areas are the places which generate economic dynamism, breaking this vicious cycle is at the heart of creating this in developing countries. As property tax is the most suitable source of revenue of local governments, its reform is critical to breaking this vicious cycle.

The economic analysis based on the partial equilibrium and general equilibrium has three kind of views:

**1.The tradition view**

The tradition view adopts a partial equilibrium approach, argues that the property tax imposed on the local housing market is shifted forwards to the consumer of in the forms of higher housing price under certain assumptions (e.g., in the framework of the standard small open economy, national return to the capital fixed). So, there is no tax on the capital, and impose of property tax will result in higher price of the house. The benefit view concludes that the property tax is simply a payment of local public service received; the capital tax view believes that the property tax is a distortionary tax on the use of capital with a local jurisdiction. The benefit view is based on the Tiebout model of local government initiated by Hamilton and Fischel since 1970s. The Tiebout model concludes that the efficiency of resource allocation can be reached by the consumer mobility (consumer of the local public service can vote with feet for alternative combinations of local tax and expenditure) and inter jurisdictional competition. So, basically the local tax is a price paid for the local public service. Later, Hamilton and Fischel applied the theory to the local property tax. Under certain assumptions (local government can use zoning constraint to maintain the minimum value of the house, etc.), they believed that the property tax is a user charge that paid in return for the benefits of local service, it is non-distortional tax; as a benefit tax, the property has no effects on the distribution of income.

**2.TheCapital Tax view**

The traditional view is regarded as a special case of the capital tax view, as the latter explained the tax incidence in a more general aspect and in the long run while the first view only on the partial equilibrium framework and in the short run. Also, the capital tax view and benefit view both predicts that the full burden of an increase in the property tax will be burdened by the local residents. However, the difference of the two view is that, the former believes that the property tax is distortionary tax on capital and have distributional effect while the latter is believe to be a non-distortionary tax and have no distributional effect.

The capital tax view was proposed by the Mieszkowski and Zodrow in 1970s. It applied the Harberger general equilibrium model to illuminate the tax incidence of the property tax. They argue that the property tax is a distortionary tax on the local use of capital, which result in the misallocation of national capital stock across local jurisdiction. The increase of the property tax may result in two economic effect, the profit tax effect and the excise tax effect. The profit tax effect is illuminating as the average burden of all property tax imposed across the nation assumed by the capital owner generally, which result in the property tax to have some degree of progressivity; the excise duty effect refers to the situation that the property tax differentials about the national average will result in the form of housing and commodities price increased and the wages and land prices declines in relatively high tax jurisdiction, vice versa.

**3. The Musgrave-Oates tradition**

In the Musgrave-Oates tradition, in a multilevel fiscal system, assignment of functions and sources of finances according to comparative advantage implies that macroeconomic stabilization and redistribution should be predominantly a central responsibility and local governments would have principal role in the allocation function **(Oates, 1972).** This implies that all broad based and progressive tax bases go the Central government and local governments will have to carry out large and growing expenditure responsibilities. This could result in excessive dependence on federal transfers resulting in softening of the budget constraints and severing of the relationship between revenue-expenditure decisions or local governments carrying on unfunded mandates resulting in poor service delivery. Either of these outcomes would imply adverse implications for efficiency and accountability. Empowering local governments would imply avoidance of heavy transfer dependency, imposing a hard budget constraint and ensuring adequate resource handles for the provision of public services the local governments are mandated to provide. Therefore, an important implementation rule of fiscal decentralization is that there should be a strong

'Wicksellianlinkage' –the linkage between revenue and expenditure decisions **(Breton, 1996).** This linkage ensures transparency and the taxpayers force the governments to provide public services commensurate with the tax payments. Thus, according to the principles of fiscal federalism, local services, by and large, should be paid for by the beneficiaries who are the local residents. User charges are appropriate for financing locally provided services of a 'private good' nature. Local public goods should be financed paid for by the residents and the cost of financing services whose benefits spill over jurisdictions should be shared through specific purpose transfers. A local tax designed to satisfy these requirements should in principle have the following characteristics **(Bird 2006):**

(i)The base should be relatively immobile to allow the local authorities to vary the rates without losing the base.

(ii)The tax should yield adequate revenues to meet local needs and should be sufficiently buoyant over time.

(iii)The tax should be stable and predictable over time.

(iv)It should not be possible to export the tax burden to non-residents except to the extent that such burdens capture benefits non-residents obtain from local services.

(v)The tax base should be visible to ensure accountability.

(vi)The taxpayers should perceive the tax to be reasonably fair.

(vii)The tax should be relatively easy to administer

From economic efficiency point of view, it is argued that less responsive (to taxes) tax bases should be taxed at higher rate. The businesses are more responsive (mobile) than the residents and therefore, should be taxed at lower rates. However, most municipal governments find it easier to levy heavier taxes on non-residential properties as this is an easy way to shift the tax burden to non-residents.

**4.The General Equilibrium Incidence view**

The general equilibrium incidence view on property taxation is that capital is mobile, but is fixed in supply and therefore, the incidence falls on the owners of capital **(Mieszkowski and Zodrow, 1989).** However, in the long term, capital immobility is not extreme and it is possible to shift a part of the burden. Furthermore, when the tax is levied on non-residential (commercial and industrial) properties, the tax may be shifted forward to the consumers of products or shifted backward to labour depending upon price elasticity of demand for the products and factor intensity and substitution. In this situation, it is not possible to conclude that property tax is definitely progressive. It is also possible that the local governments may

use the non-residential property taxes more heavily to export a part of their tax burden to non-residents and the incidence of this component is difficult to ascertain.

Despite the difficulties and sometimes, the unpopularity of the levy, the world over, taxes on immovable properties have been the mainstay in financing municipal services. The study by **Bahl and Martinez–Vazquez (2008)** shows that (i) property tax is a significant source of revenue for local governments both in developed, developing countries as well as transitional countries. (ii) In terms of percentage to GDP, the contribution of property tax in OECD countries was over 2 per cent whereas, it was about 0.6 to 0.7 per cent in developing and transitional countries. (iii) In the case of developing countries, the contribution of property tax remained has not shown any appreciable increase both as a ratio of GDP and as percentage of total expenditures of local governments.

Empirical studies show that the volume of property tax collection depends on the level of development of the country and the extent of its fiscal decentralization **(Bahl and Martinez-Vazquez, 2008). Sennoga, Sjoquist and Wallace (2008),** using a computable general equilibrium model with a large informal sector and less than perfect mobility of capital –the structural features to represent developing a transitional country show that the burden of property taxes is primarily borne by owners of land and capital and thereby the distribution of tax burden is progressive.

**Review of Literature**

This section deals with the review of literature related to municipal property tax.A good deal of work has been done on municipal finances and local government. Many studies have focused on the Political organization and financial administration and the fiscal dimensions of these local bodies. A few of the relevant works have been reviewed here high lightening their major thrust on the financial analysis of the municipal corporations in different parts of the country. The collection of reviews is a comprehensive survey of the literature which is done by the academicians, practitioners, researchers, etc. The review of literature enables the researchers to find the research gap and chosen the amenable methodology under the light of limitations of various available estimation procedures, database, lucid interpretation and reconciliation of the conflicting results.

- **Oates, (1969)** observed that the tax assumes the role of a quasi-benefit charge and therefore, is more acceptable and thus evokes greater degree of compliance. The property tax takes the character of a benefit tax as owners of property benefit from public services provided by the local governments. It is also argued in the literature that fiscal

differentials at the local levels get capitalized into property values**.** This characteristic of the tax also makes it a progressive tax.

- **AbhijitDatta (1971)** reviewed the existing position of State-Municipal grants and shared taxes in India. His study pointed out that the reasons for rapid growth of grants to the State Governments are; (a) the launching of the Five-Year Plans at the national level that necessitated large-scale plan grants to the states and (b) the awards of the Successive Finance Commissions which stabilized the pattern of statutory grants to the states. He concluded that the existing institutional vacuum for allocating state grants and shared taxes to the local authorities remains to be corrected through the periodical examination of these issues by state-appointed finance or grants commissions. The Federal Finance Commission and the Planning Commission also must take into consideration the issue of state assistance to local government so that the latter finds a place in national decision-making and financing.
- **Khurana (1971)** studied the municipal property taxation and Urban Development. He found that the present system of Municipal Property taxation is weak in all regards rates, basis, assessment procedures, valuations, collection and administration. He also suggested that the system of municipal property taxation would require substantial improvements so far as the basis of assessment and overall administration is concerned. More than this, efforts will also have to be made to so broaden and widen the municipal property tax that it will not only effectively mop up unearned increase in values of urban land and properties, but also become a lucrative source for financing urban development.
- **Rama Rao (1974)** has made a study of Municipal Revenue in Andra Pradesh. His study analyzed the major sources of municipal revenue including tax and non-tax revenue and grants-in-aid. He observed that taxes constitute a promising source of revenue and a large bulk of revenue is sacrificed for want of better administration. He found that with the imaginative changes in the administration of major taxes, the municipal bodies can derive substantial revenue. He also gave the suggestions regarding revenue assignments, grants-in-aid and capital planning.
- **Sundaram (1981)**in his article "Municipal Finance and the levy of Property taxation" found that the revenue from the property tax is dependent on three major points (a) the levy of the tax, its rates and limits of exemption (b) proper assessment and its regular periodic revision and (c) proper collection. He observed that there is considerable variation in the rates of property tax levied in different states. The rates are generally high

in Kerala, Tamil Nadu, Andhra Pradesh and Bihar varying from 25 to 40 percent. The rates are also quite high in Ahmadabad and Bombay. He pointed out that, it would be necessary to remove the restriction on rates of taxes in the form of maxima and exemptions limits. He concluded that the property tax accounts for a considerable proportion of the total revenue of the income of municipal bodies in different states.

- **ShyamNath (1983)** made an attempt to study the property tax potential of major municipal corporations in India. He analyzed the five major corporations like Ahmedabad, Bangalore, Bombay, Calcutta, Delhi and Madras. He emphasized that the rising expenditure requirements would largely determine the extent of tax base utilization of all revenue source. The results show that five out of six major municipal corporations have not utilized the potential property tax base adequately if their performance is judged in the context of a representative rate. The performance of the Bombay Corporation shows that a proportionately higher tax rate is likely to compensate for the loss of revenue on account of low assessment ratio. Finally, he concluded that the main constraint on the improvement of civic services in the major municipal corporations is lack of financial resources. His study revealed that the existing property tax system has not been able to adequately utilize the property tax base and more than half of the potential tax remained untapped. He suggested that the upward revisions of the rateable value, the properties automatically move to higher rateable value groups with higher tax rates.
- **M.P.Sharma (1984)** in his article "Collection of Property Taxes: A Case Study of Delhi", has made a study of collection of property taxes of Delhi Municipal Corporation. He observed from his study that, the property taxes are the major sources of revenues to the municipal Corporation of Delhi. The total collection of revenue from property taxes was approximately 54 percent of the total municipal revenues. He also observed certain basic shortcomings in the legal provisions. He pointed out that no provision for levy of interest on delayed payments which provides allurement to the business minded tax-payers for utilizing municipal revenues for their profit-making endeavours.
- **Raju (1986)** in his article "Case Study of Three Urban Local Bodies Some Implications for Urban Finances in India" made an attempt to study the financial structure of the three municipal bodies namely the Chennai Corporation, Bangalore Corporation and Mandya Town municipality. He found that the major source of revenue for these three urban local bodies has been property tax. He observed that the state government's interference in the municipal finance had affected adversely the state-local relationship. He also suggested a

number of measures to improve the property tax revenue. Besides, the study has pointed out that the share and magnitude of loans and grants in the revenue source is increasing.

- **ChetanVaidya and Basu (1986)** in their article '"Revenue Base of Secondary Cities of Tamil Nadu – A Review"' have analyzed the Revenue Base of Secondary Cities of Tamil Nadu. They have analyzed four urban local bodies like Madurai Municipal Corporation, Coimbatore Municipal Corporation, Trichy Municipality and Salem Municipality during 1980-81 to 1984-85. They found that property tax and professional tax dominate the own source of revenue of the urban local bodies. They also found that there has been a significant growth in revenue form entertainment tax in the above urban local bodies. Madurai Municipal Corporation has been the lowest in the realization of own source of revenue from property tax and professional tax among the other three municipal bodies. They also suggested revision of tax rates and tax bases, introduction of new revenue raising taxes, periodic assessment of property valuation and collection of more shared revenues from the state government.
- **Bahl and Linn, (1992)** noted that exemptions have been criticized on a number of grounds: First, to the extent that people working in government buildings or institutions use municipal services just as workers do in other buildings, they should be taxed.
- **Dillinger (1995)** stated that ' the low yield of the property tax is, in an immediate sense, the combined result of inappropriate policy and poor tax administration' and also stated (Dillinger, 1991) that 'given the extremely low level of collection efficiency in developing countries , much of the effort spent in mapping and valuation is likely wasted if corresponding efforts are not made to improve collection administration: newly discovered and valued property does not yield revenue if the system of collection administration is dysfunctional.
- **Netzer, (1998)** stated that property is a heterogeneous good. Its value reflects economic, social, physical, and legal factors. Accurate assessment is the benchmark of a good property tax administration. The purpose of assessment is essentially to determine the 'fair market rental' or 'fair market value' of the property.
- **McCluskey, (1998)** recognised **t**he importance of the property tax as a source of financing tends to be overlooked because fiscal analysis normally focuses on central government or state finances, and in that context the property tax is a relatively minor source of revenue

- **Sita Sekhar and Smita Bridarkar (1999)** have analysed the budgets of the corporations of the five cities of Ahmedabad, Bangalore, Chennai, Mumbai and Pune using the budget data. They observed that there is substantial growth in terms of population, and area under the jurisdiction of the municipal corporation. It would be presumed that revenues and expenditures would have grown as well. They found that octroi and property tax constitute the two major sources of income for all corporations while octroi forms 60 to 70 per cent of the total revenue for the cities that levy octroi. For Bangalore compensation forms an average of only 20 per cent of the revenue annually. In case of Chennai, Octroi has been abolished years ago and no specific compensation is provided by the state government. On the expenditure side, grants and administrative expenditure form the largest chunk of Ahmedabad's expenditure. Mumbai Corporation spends the largest portion of expenditure on solid waste management and public health. Bangalore Corporation spends more on health and public works. In Pune Municipal Corporation, education is the most important component of its expenditure incurred by the corporation on paying salaries to their employees that makes up a large chunk of the total expenditure. They suggested measures such as modernization, computerization of information system, setting up goals and ensuring accountability in expenditure.
- **Kelly, (2000)** believed that despite the relatively low contribution of property taxes to national revenue, virtually all countries seem to be focusing on strengthening the property tax, the most common revenue source for local governments throughout the world.
- **Bird (2001)** observed that the local government is interested on revenue from property taxes to finance local social services provision to the people. Property tax has an opportunity to enhance public fiscal policy decision on local government expenditure therefore is required by the local Government.
- **Fischel (2001)** argued that the property tax in the United States is like a benefit tax because taxes approximate the benefits received from local services. Contrast to the benefit view, many see the property tax as a tax on capital or, to the extent it falls on housing, as a tax on housing services.
- **Zodrow (2001),** argued that the property tax in the United States results in distortions in the housing market and in local fiscal decisions. Home owners who improve their houses for example, will face higher taxes as a result and will thus be discouraged from doing so. Property tax is believed to be a major contributor to annual budgets of many local authorities in the developed countries.

- **Bird and Slack (2002)** have analysed that the reasons for the relevance of considering property tax as most appropriate tax for local governments: **o**ne reason that taxes on land and property have been considered to be especially appropriate as a local revenue source is that real property is immovable-it is unable to shift location in response to the tax. Another reason is the connection between many of the services typically funded at the local level and the benefit to property values.
- **Mohanty (2003)** found that although tax reforms and strategy depend on the "pre-conditions" certain factors like close involvement of the tax paper, tax-service linkage, incentives for filing of tax returns, disincentives for non-filing, tax education are very important. The study claims that although it is useful to have uniform slab rates for homogeneous properties, it can be regressive in case of heterogeneous properties.
- **Madon et al (2004)** looks at the Bangalore City Corporation's (BCC) initiative to reform its property tax system and the interaction between the "local contingencies" and "external influences" in implementing such reforms. Although in nominal terms, property tax revenues have grown by 10.4per cent from 1988-1994-95, the inflation adjusted figures reflect stagnation.
- **Lall and Deichmann, (2006)** throws some light on the issue for two states Karnataka and Maharashtra, with Bangalore and Pune as the study sample, they found that there forms that get the property tax base closer to the market value have significant and positive implications for revenue generation.
- **Bird and Slack (2007)** review the various possible candidates for local taxes and consider that the most appropriate tax at the local level is the tax on real properties. There are a number of advantages of assigning the property tax to local governments. The tax base is large and if properly designed, these can be elastic and productive.
- **Mohanty et al (2007)** observed that various reforms agenda prescribes changing over to valuation based on unit area characteristics, there is a view which challenges the faith in the market-based valuation system in India as there is no clear-cut definition of a "market value" which might harm the tax yields (Mathur et al 2009).
- **Sennoga, Sjoquist and Wallace (2008),** using a computable general equilibrium model with a large informal sector and less than perfect mobility of capital –the structural features to represent developing a transitional country show that the burden of property taxes is primarily borne by owners of land and capital and thereby the distribution of tax burden is progressive.

- **Smoke, (2008**) examined that a major problem with the property tax administration in municipal bodies is the poor information on property tax base with them. The important pre-requisites for efficient property tax system are that there should be clarity in property ownership or tenancy rights and a cadastre that uniquely identifies properties and their owners. In addition, there should be appropriate mechanisms for periodic market-based valuation of properties and systems and processes for tax collection and enforcement.
- **Bahl and Martinez–Vazquez (2008)** revealed that despite the difficulties and sometimes, the unpopularity of the levy, the world over, taxes on immovable properties have been the mainstay in financing municipal services. Empirical studies show that the volume of property tax collection depends on the level of development of the country and the extent of its fiscal decentralization**.**
- **Roy (2009)** stated thatinternally, the increasing demand of public services and the local government need to finance some of its project by revenue from property tax making it an issue of concern globally that decussated many countries to impose tax on real property.
- **Mathur, (2009)** made a study on the Indian tax, recognized the defects and problems in the property tax system. The study shows property tax revenue is low, caused by; restriction on tax base due to the large amount of statutorily discharged property from tax, high rate of tax violation and weakness in rule of law and regulations, weakness in the system of property valuation, old tax rate structures.
- **Gnaneshwar, (2009)** in his study based on municipal corporations from Andhra Pradesh, Tamil Nadu and Karnataka establishes that the gain in Karnataka from moving to an area-based tax system has been the most because of the fact that in Karnataka, the reform has been executed with a revision in the legal framework whereas in the other two states the existing legal provisions were used.
- **Bird and Slack (2004), NIUA (2010)** viewed that mobilising revenues through property tax in an equitable and efficient manner is the ultimate goal of a local government. Once the legal tax base is identified and values of the properties are estimated, tax rolls can be created by applying the tax rates which gives the potential tax revenues. Once they are collected, the potential can be actually realized. Collection ratios vary across countries. In most OECD countries they are close to 100 per cent while in non-OECD countries they can vary between 30 and60 per cent.
- **Mathur (2009) & NIUA (2010)** stated that the local governments can follow a partnership approach where the tasks of collection, updating and maintenance of

information on properties and taxpayers can be outsourced to an agency. Valuation of properties is an important issue. Valuation can be done based on the capital value, rentals or area of the properties. While capital values are subject to market fluctuations, rent controlled properties create distortions in the rental value-based methods. Valuation based on unit area characteristics are safer options with less fluctuations. Many developing countries have opted for unit area-based valuations.

- **Mosha (2010)** viewed that in a traditional point of view, property tax has been identified with local government for reasons of its visibility and the inability of the tax object to shift location as a result of the imposed tax.
- **Slack, (2011)** found that there are severe problems associated with determining the values of immovable properties, particularly in developing countries. Visibility of the tax and often, lack of association between the tax paid and benefits from local public service received makes the tax unpopular.
- **Slack, (2012)** revealed thatEconomics commands that property tax ought to be levied to reach to some public finance principles like equity and efficiency. The reality of how property taxes are employed in the countries, however, is often much different from what those principles would recommend.
- **Kelly (2013)** observedthat to enhance collection ratios, voluntary compliance has to be ensured. Incentivizing tax payments is important. Providing discounts for timely payments is one option. Establishing a strong link between property tax payments and public service delivery is another. A combination of policy and administrative reforms are needed to deal with tax base coverage, property valuations, collections, enforcement and taxpayer services.
- **McCluskey et al., (2013)** viewedthat the most critical and integral factor of any tax system is the determination of tax rate, such as wealth, income or consumption. The question raised how the tax rate imposed on the property to mobilize the government revenue, it fairness and administrative costs of tax authority. Generally, a tax system formed by the establishing law as a general guidance for what property ought to be the subject of taxation, how it to be valued, setting the rule and regulations for tax authority, discovering property, preparing a record of property, calculation of property value, defining the taxable value of the property, creating the tax rate and calculation the bill of tax for subjected property.

- **Bandyopadhyay (2013)** compares the implementation of the property tax reforms in two major metropolitan cities in India, Delhi and Bangalore. Both the cities have implemented the property tax reforms and have shifted to the unit area method of assessment. However, while property tax collection rose for Bangalore after the implementation of the reforms, Delhi experienced a fall in the number of properties assessed and property tax collection after the implementation of the reforms.
- **Sexton (2014)** found that tax burden is a significant matter in the subject of property taxation. Typically, the classification system makes property tax relief to the landlord of specific kinds of property. To redistribute the burden of tax among different categories of property make incentive in the usage of certain kinds of property.
- **Banerjee, (2017)** made an empirical study about the role of municipal corporation in India has been done by Banerjee. The study evident the significance of public service provision in urban area, the development of India in the lung-run will incomplete without the provision of important municipality's services.
- **Collier et al, (2018)** found that municipal property tax is characterized by the numbers of key features. The most significant of them are: first, Tax of municipal property is often fair than other kinds of tax. It means when local government spends on public services like road building, schools, near to the propertied which are taxed by government, the price of these properties significantly rise. Further, the value of the land in that city and localities increasedue to the increasing government spending, urban development and population growth. The second benefits often than other taxes, related to the returns on government investment form public services and infrastructure. These types of government investments on public services and goods increase the value of assets in subjected area like the project of water supply and so on, such projects generate the stream of income for government to implement large project. Third, fixed amount of land in the city paves the way for efficient use of property in city. Fourth, as properties are immovable and highly visible, thus it is easy to identify, levied the tax and monitor it.

**Research Gap**

- The above review of literature survey highlights the various studies made on the collection and progressivity of Municipal Property tax across the selected metro cities in India.
- Though Substantial amount of works were done by different scholars in this field, almost the studies were focused on the analysis of a particular state. This study attempts to fill

this gap by studying the overall performance of Municipal property tax in major selected cities of India.

**Profile of the selected cities of the study area**

**Greater Bangalore Municipal Corporation**

Since Bangalore is the capital of the State of Karnataka and is one of the biggest Municipal corporation in India with regard to collecting highest property tax in India, the research tries to find out the impact of property tax in Bangalore Municipal corporation. The BBMP was formed out of seven City Municipal Councils, one Town Municipal Council, and one hundred and eleven villages in the Bruhat Bangalore MahanagaraPalike. While the urban area tripled by the amalgamation (from 226 to 756 sq. km) the population increased from 4.5 to 5.6 million. The property tax of Bruhat Bangalore MahanagaraPalike (BBMP), which is translated as the Greater Bangalore Municipal Corporation, is defined within the Karnataka Municipal Corporation Act 1976 (KMC Act 1976).

**Greater Chennai Corporation**

The Greater Chennai Corporation (previously Madras) is the Oldest Municipal Institution in India established on the 29th September 1688. A charter was issued on the 30th December, 1607 by East Indian Company constituting the "Town of Fort St. George" and all the territories thereunto belonging, not exceeding the distance of ten miles from the Fort, into a Corporation. The Parliamentary Act of 1792 gave the Corporation power to levy Municipal Taxes in the City. The Municipal administration properly commenced from the Parliamentary Act, 1792 making provision for the good order and administration of the city. The Municipal Act has been amended introducing from time-to-time major changes in the constitution and powers of the Corporation. The Madras Municipal Corporation Act, 1919 (as amended) provides the basic Statutory authority for the administration now. The Council of 200 councilors is headed by the Honorable Mayor and Council meets ordinarily once in a month. The executive wing is headed by the Commissioner. There are Deputy Commissioners and various Heads of Departments and 15 Zonal Officers at present.

Chennai is located on the Coromandel Coast on the Northern end of the State of Tamil Nadu. The city stretches along the Coromandel Coast much of its superb sandy beach and extends inland. Its irregular shape covers about 426 Sq. Km. The estimated present population of Chennai is 7.1 Million. Over the years, the City has developed in trade, commerce and

industry. Chennai City is the biggest industrial and commercial centre of South India. There are about 15,000 industries and factories licensed in the Chennai City. The Annual Budgetary estimate of Greater Chennai Corporation in 2012-13 revenue is 1326.11 crores and expenditure is 1232.97 crores. Surplus income is 93.14 crores.

**Municipal Corporation of Greater Mumbai**

The Municipal Corporation of Greater Mumbai formerly known as the Bombay Municipal Corporation, is the governing civic body of Mumbai, the capital city of Maharashtra. It is India's richest municipal corporation. The MCGM's annual budget exceeds that of some of India's smaller states. It was established under the Bombay Municipal Corporation Act 1888. MCGM is responsible for the civic infrastructure and administration of the city and some suburbs. The Mumbai Metropolis has a historic tradition of strong civic activism dedicated to the cause of a better life for all its citizens. And it's the Municipal Corporation of Greater Mumbai (MCGM), the primary agency responsible for urban governance in Greater Mumbai. From the time of its establishment in 1882 as India's first municipal corporation, numerous non-political groups, NGO's and organizations of citizens have worked closely with the civic body in the fields of education, public health, creation of urban amenities, art and culture, heritage conservation etc. MCGM is one of the largest local governments in the Asian continent.

**Kolkata Municipal Corporation**

Kolkata Municipal Corporation, formerly Calcutta Municipal Corporationis the local government of the Indian city of Kolkata, the state capital of West Bengal. This civic administrative body administers an area of 206.08 square kilometers (79.57 sq mi). Kolkata Municipal Corporation was established in 1876. Each borough has a committee consisting of the councilors elected from the respective wards of the boroughs. The Corporation, through the borough committees, maintains government-aided schools, hospitals and municipal markets and partakes in urban planning and road maintenance.The corporation as the apex body discharges its function through the Mayor-in-Council, consisting of a mayor, assisted by a deputy mayor, and ten other elected members of the KMC. The mayor is responsible for the overall functioning of the KMC and has a tenure of five years.

**Pune Municipal Corporation**

The Pune Municipal Corporation is the civic body that governs the inner limits of Pune, India. It is in charge of the civic needs and infrastructure of the metropolis, which is spread

over an area of 484.61 sq. km. and has 3.4 million residents. Property tax is a levy issued by a government on a person's real or personal property. The property is assessed to give it a value and then that value is taxed. The amount of tax owed is determined by multiplying the fair market value of the property by the current tax rate.

**Calculation of municipal Property Tax**

Property tax is calculated by the municipal authorities in proportion to the assessed value of the property. There are mainly three ways of calculating property tax:

**Capital Value System (CVS):**

The tax is levied as a percentage of the market value of the property. This market value is determined by the government and is based on the locality of the property. The market value is revised and published yearly. Mumbai follows this system.

**Annual Rental Value System or Rateable Value System (RVS):**

Under this system, the tax is calculated on the yearly rental value of the property. This is not necessarily the actual rent amount being collected; rather it is the rental value decided by the municipal authority based on the size, location, condition of the premises, proximity to landmarks, amenities etc. Examples of municipalities following this system of property tax include Hyderabad and Chennai.

**Unit Area Value System (UAS):**

In this system, the tax is levied on the per unit price of the built-up area of the property. This price is fixed (per square foot per month) based on the expected returns of the property as per its location, land price, and usage, and is then multiplied with its built-up area. Municipalities like Delhi, Kolkata, Bengaluru, Patna and Hyderabad follow this system for property tax calculation.

## The formula used for calculating property tax is given below:

**Property tax = base value × built-up area × Age factor × type of building × category of use × floor factor**

Property tax in India depends on the location of a property in question, with taxes varying from state to state. Different civic corporations use different methods to calculate tax, but the general overview of such calculations remains the same and is explained below.

An assessment of the property is first carried out by determining the area it is in, occupancy status (whether it is self-occupied or rented out), type of property (residential, commercial or land), amenities provided (car park, rainwater harvesting, store, etc.), year of construction, type of construction (multi-storied/ single floor/ pukka or kutcha structure, etc.), Floor space index and carpeted square area of the property.

Once these parameters are determined the civic agency can use a formula it deems fit to calculate tax. Different agencies use different formula.

The tax on a property will vary according to the factors mentioned above and can be easily computed online, through the official website of the municipal corporation concerned.Some would say that India is in a state of flux about how it should tax property, and in fact thereare several choices about how to do this. Property taxes are based on

(i) Annual Rental Value (ARV) of the property,

(ii) Capital value (CV) of the land and improvements, and/or

(iii) Site value of the land.

Most Indian cites use ARV as the base of the property tax. Although a few cities have adopted a CV base (including those in Karnataka, for example), implementation of the capital value system has not begun. The property tax base in Indian ULBs is more appropriately described as being the rental value of property. Various ULBs in India have adopted a unit value system (sometimes referred to as an area-based system), which in essence is a combination of the ARV and CV systems. In the unit-value system, values per unit of land (usually per square foot) are estimated and the tax base is the product of this unit value and land area, plus the value of the structure. The latter is determined in an analogous way: a basic value per square foot is determined, weighted by construction quality and multiplied by area. This method has been used as a way to get around the limitations imposed on the property tax base by rent controls, or perhaps as a transition to a capital value system.

**Different Methods of Calculating Property Tax**

In general, the municipal authorities use one of the following 3 methods for the purpose of calculation of property tax:

1. **Capital Value System (CVS):** Under the Capital Value System (CVS), the property tax is calculated as a percentage of the market value of the property. The market value of the property is decided by the government on the basis of the locality of the property. This valuation system is followed in the city of Mumbai.
2. **Unit Area Value System (UAS):**

The tax valuation as per the Unit Area Value System or UAS is calculated on the basis of the per unit price of the built-up area of the property. This price is decided on the basis of the expected returns of the property as per its location, usage, and land price. This value is further multiplied with the built-up area of the property to derive the tax valuation. A number of municipal authorities such as Patna, Bengaluru, Delhi, Hyderabad, and Kolkata follow this method.

3. **Annual Rental Value System (ARV) or Ratable Value System (RVS):**

As per the RVS or the Annual Rental Value System, the tax is calculated on the rental value which is derived from the property in a year. This need not be the actual rent amount which is collected from the property. However, it is the valuation of the rent which is determined by the municipal authority and is derived on the basis of the location, size, and condition of the property. The proximity of the property to landmarks and other relevant amenities is also taken under consideration at the time of valuation. Chennai and parts of Hyderabad follow this method of tax calculation.

Most cities in India are based on Area Rental Value assessment, which is mostly defined as "gross annual rent of land and buildings at which they might reasonably be expected to let from year to year" (Bagchi2003: 4482). The term 'reasonably' involves a great deal of room for interpretation. Due to missing information on the rental values of properties, it has become an "assessors and valuers paradise" (Bagchi2003: 4482). Rental values are estimated by inspectors based on a set of internal guidelines and a visual inspection of each property. Furthermore, Rent Control Laws are implemented, referring to 'fair rent' or 'standard rent', which have set limits on a 'reasonable' rent. Rent Control locked the rental value over time to unrealistic low values. Both, Rent Control and discretionary powers of authorized officers had important implications on the overall tax revenue generation and the tax burden among the taxpayers. Therefore, several cities reformed their property tax systems by moving toward the Capital Value System. Generally, Rental Value (income) and Capital Value (wealth) are the same, i.e. if property is put to best possible use; in this case, the net stream of rental payments discounted to the present value approximates the current capital value of the property. The property tax of Greater Mumbai is based on the capital value system, which constitutes at the same time the tax base for several other taxes. According to the Mumbai Municipal Corporation Act, the property tax is divided up into the General Tax (including fire tax), Water Tax, Water Benefit Tax, Sewerage Tax, Sewerage Benefit Tax, Education Cess, and Street Tax (Section 139).

The property tax payable in Greater Bangalore is based on Unit Area Value (which features assessment under the capital value system according to Gosh and Kundu2011: 109; and is referred to as quasi-capita system by Lall and Deichmann2006: 5) with 20% tax rate applied. Beyond that, on the tax payable, another 15% Health Cess, 6% Library Cess, and 3% Beggary Cess are applied constituting the gross property tax payable.

Municipal Corporations collect several million bits of information in the data inventory for property taxes. The use of information technology has made the storage of these massive chunks of data more accessible and affordable. Digitization of tax rolls has been carried out by all the six largest Municipal Corporations. To improve collections Municipal Corporations must develop an integrated system to automatically record changes in ownership, property division and consolidation, changes in property use, development of a new road, and additions and alterations to existing property. Such an integrated system, shared across departments of the Municipal Corporation, can create economies and reduce costs.

Three systems of property valuation are practiced among the Municipal Corporations in India – Annual Rental Value System (Chennai, Hyderabad), Unit Area Value System (Bengaluru, Ahmedabad, Kolkata), and Capital Value System (Mumbai).Once the taxable base has been determined, the next step is to determine the value to which the tax rate is to be applied. In general, two distinct assessment methodologies are used for property taxation: area-based assessment and value-based assessment, with the latter being divided into capital and rental value approaches. In addition, some countries use a system of self-assessment.

For most Municipal Corporations the band for property tax rates are set by the state government or by the Corporations with the approval of the state government. Tax rate revisions are often met with political resistance.

- **Area-based Assessment**

Under an area-based assessment system, a charge is levied per square meter of land area, per square meter of building (or sometimes "usable" space), or some combination of the two. Where measures of area are used for both land and buildings, the assessment of the property is the sum of an assessment rate per square meter multiplied by the size of the land parcel and an assessment rate per square meter multiplied by the size of the building. The assessment rates may be the same for land and buildings, or they may be different. For example, a lower unit value per square meter might be applied to buildings to encourage development.

A strict per unit assessment results in a tax liability that is directly related to the size of the land and buildings. With unit value assessment, the assessment rate per square foot is adjusted to reflect location, quality of the structure, or other factors. Market value has an

indirect influence on the assessment base through the application of adjustment factors. For example, the assessment rate per square meter might be adjusted to reflect the location of the property within a particular zone in the city. Although the specific location of the property within the zone is not taken into account, properties in different zones will have different values.

The adjustment factors are derived from average values for groups of properties within each zone and do not reflect the characteristics of each individual property. When the groups are defined narrowly enough, however, unit value begins to approximate market value. For example, a zone could be defined anywhere from an entire city to specific neighbourhoods to properties on one side of a street.

- **Market Value Assessment**

Market value (or capital value) assessment estimates the value that the market places on individual properties. Market value is defined as the price that would be struck between a willing buyer and a willing seller in an arm's length transaction.

The following methods are used to estimate market value:

The comparable sales approach looks at valid sales of properties that are similar to the property being assessed. It is used when the market is active and similar properties are being sold.

The depreciated cost approach values the property by estimating the land value as if it were vacant and adding the cost of replacing the buildings and other improvements to that value. The cost approach is used when the property is relatively new, there are no comparable sales, and the improvements are relatively unique. The cost approach is also normally used to assess industrial properties.

Under the income approach, the assessor estimates the potential gross rental income the property could produce and deducts operating expenditures. The resulting annual net operating income is converted to a capital value using a capitalization rate. This approach is used mainly for properties with actual rental income.

- **Rental Value Assessment**

Under the rental value (or annual value) approach, property is assessed according to estimated (not actual) rental value or net rent. One rationale for using rental value is that taxes are paid from income (a flow) rather than from wealth (a stock) and thus it is appropriate to tax the net rental value of real property. In theory, however, there should be no difference between a tax on market value and a tax on rental value. When a property is put to its highest and best use and is expected to continue to do so, rental value will bear a

predictable relationship to market value – the discounted net stream of net rental payments will be approximately equal to market value. This relationship does not always hold, however. First, gross rents are often used rather than the economically relevant "net" rents that build in an allowance for maintenance expenditures, insurance costs, and other expenses. Second, most countries tend to assess rental value on the basis of current use. There can thus be an important difference between market value and rental value. A property that is under-utilized – that is, currently used for a purpose less productive than other possible uses -- would be assessed much lower under the rental value approach than under the market value approach. From a land use perspective, a tax based on value in highest and best use is more efficient than a tax based on current use because it stimulates use to its highest potential by increasing the cost of holding unused or under-used land (as compared to developed land).

There are some problems with the use of rental value assessment. First, it is difficult to estimate rental value when there is rent control. Controlled or subsidized rents cannot be directly used to assess market rents unless the majority of properties are rent controlled. This has been an important problem in India, as discussed in that case study. Second, because vacant land is not taxable under a tax based on rental value in current use (since there is no current use!), an incentive is created in favor of low return uses over high return uses and to withhold rental properties from the market altogether. If vacant properties are not taxed, the tax has to be higher on occupied properties to yield the same amount of revenue. These higher taxes further discourage investment. In terms of the administration of the tax, there are some additional difficulties with using rental value.

First, rental value is difficult to estimate because there is not much information on the annual rent of comparable properties for unique commercial and industrial properties such as steel mills, for example. Second, it is difficult to calculate net rents because the distribution of expenses between landlords and tenants differs for different properties. Third, assessors may not have access to rental income information because rental income is not always in the public domain in the same way as are sales prices.

- **Area-based vs. Market-based Assessment**

Where it is possible to use market value, it is generally regarded as a better tax base. First, the benefits from services are more closely reflected in property values than in the size of the property. For example, properties close to transit systems or parks enjoy higher property values. The benefits from these services are not reflected in the dimensions of the property but rather in the value of the property. Even those services where the benefits may relate

more closely to property dimensions (such as sidewalks and street lighting, for example) are related more with front footage than to lot size or building size.

Second, market value has the advantage of capturing the amenities of the neighbourhood, amenities that have often been created by government expenditures and policies. Area based assessments (particularly unit assessment) are unlikely to capture these amenities because they do not take into account differences in the quality of buildings nor their location. Consider, for example, the taxes paid by two properties of identical size and age but in different locations. Specifically, one is located next to a park; the other is adjacent to a factory. Under an area-based assessment system, both properties would be levied the same property tax. Under a value-based assessment system, the property next to the park would pay higher property taxes. In this example, area-based assessments would not be fair.

Third, area-based assessment results in a relatively greater burden on low-income taxpayers than high-income taxpayers when compared to value-based assessment. The reason is that average household incomes in high-value neighbourhoods are higher than in low-value neighbourhoods. A tax on area taxes all properties that are the same size the same amount, whether they are in high-income or low-income neighbourhoods. Similarly, older houses in a bad state of repair but with a large floor area will pay relatively high taxes.

- **Self-Assessment**

Self-assessment requires property owners to place an assessed value on their own property. In Hungary, for example, the current local tax system is based on the principle of self-identification. Taxpayers are obliged to register and report their tax obligations to the local tax administration. The verification for the tax on buildings and tax on idle land in Hungary requires verification only of the property size and not its market value. In practice, the responsibility of self-registration is not particularly effective because not all owners comply. Consequently, the number of potential taxpayers or taxable assets is generally unknown. The determination of tax liabilities also requires verification of the self-assessment submitted by the taxpayer. The lack of personnel to make field inspections of each property in Hungary means that verification is inadequate.

**Municipal Property Tax Reforms**

Cities drive economic growth by catalyzing agglomeration and network externalities. These externalities are responsible, among other things, for cities being the engines of growth and structural transformation.

Property Tax Reforms in terms of the desirable criteria for choice of municipal tax, property taxes, being taxes on immobile land and buildings, are ideally suited for assignment to and

administration by the Municipalities. Further they belong to the class of general benefit taxes. They are indirect user charges for municipal services whose benefits are collective and not confined to identifiable individuals. Sometimes, property taxes are decomposed into components such as water tax, drainage tax, conservancy tax, lighting tax, fire tax, street tax, and general tax. For example, the Greater Mumbai Municipal Corporation levies the following types of property taxes: (i) General tax, (ii) Fire tax, (iii) Water tax, (iv) Water benefit tax, (v) Sewerage tax, (vi) Sewerage benefit tax, (vii) Education cess, (viii) Street tax, and (ix) Tree cess. The Municipal Corporation of Hyderabad collects property tax under the following components: (a) General Tax, (b) Conservancy Tax, (c) Drainage Tax, (d) Lighting Tax and (e) Library Cess. When property taxes collected under various components are linked to or earmarked for the services for which they are collected, they serve as indirect market prices of those services. Starting with a seminal article by the Nobel Laureate, James Buchanan (1963), a number of research papers have viewed 'earmarking' as a 'first best' operational way of dealing with the fundamental normative problem of public economics: how to provide public services that match people's preferences [Buchanan (1967), Goetz (1968), Brennan and Buchanan (1980) and Oakland (1985, 1989)]. To quote Musgrave (1992), "The principle of earmarking applies in its full sense of linking tax and expenditure determination for each program." Earmarking aims at the introduction of market prices into the budgetary process.

Some of the lessons from property tax reforms carried out by cities include the following: a. The tax system must be simple and easily understandable to the public; b. Fixation of tax should not be arbitrary; the tax rate must be linked to the tax base by a formula pre-determined by law and not subject to the discretion of any bureaucrat; c. The tax rate should be reasonably low so that compliance would be high; d. The tax system should not only be fair, but also be perceived to be fair by the taxpayers; e. The system of levy and collection should be transparent and not prone to manipulation for graft or corruption; f. The taxpayers should be involved in the decisions regarding tax reforms; tax education is critically important for the success of property tax reforms; g. The taxpayers need to be made aware that what they pay translate into services; visibility in the provision of services in the tax-paying areas enhances the willingness to pay; and h. Tax reforms should be well-timed and not be unnecessarily linked to timeconsuming processes as opportune times do not last long.

Municipal tax reforms are complex and depend on a number of factors, most of which are specific to the situations existing in the Municipalities concerned. However, some general lessons can be drawn from tax reforms in developed and developing countries. These include:

a. There is no optimal tax structure. What is optimal from the point of view of one level of government may be sub-optimal for the other levels. However, useful principles can guide tax reforms in a given situation.

b. Broadening the tax base or tax net should be given a high priority so as to avoid reliance on relatively high tax rates.

c. Tax preferences and exemptions in order to promote specific economic and social objectives - the so-called tax expenditures - need to be eliminated or reduced.

d. Tax rates should be moderate to ensure better tax compliance and to prevent tax evasion.

e. A systematic view of taxes and their institutional and political contexts is important.

f. Reforms in the tax structure and tax administration should go together.

g. Involvement in and ownership of tax reforms by the public in general and taxpayers in particular are essential for the success of tax reforms.

**Property Tax Reforms**

Almost all countries have some form of annual tax on land and property, for reasons that are well documented elsewhere but can be summarized as follows:

• It is often the main source of revenue for local government, and is an important part of the fiscal budget that supports local independence and fills the gaps between governments.

• It is economically viable because it is difficult to avoid and imposes easily when blocked.

• It is regarded as social equity because it is progressive, freely aligned with local government benefits, a good multi-year tax agent, and a way for the public sector to receive part of the private sector from the value proposition, especially due to public investment in previously undeveloped land.

Although everywhere, property taxes are looked down upon everywhere, and for reasons that are well documented elsewhere but can be summarized as follows:

• Although a large number of legal taxpayers form a large tax base, a positive thing in theory, it could be a political and administrative dream in practice;

• While high tax visibility is good for government accountability and accountability, greater awareness of taxpayers also tends to strengthen taxpayers' resilience;

• While bulk computer-assisted testing and other appropriate technologies increase efficiency and efficiency, asset measurements are still controversial;

• Although taxation is generally considered fair, there is no direct relationship between the tax debt and the ability to pay taxes, leaving some taxpayers ‘rich but poor’;

• While taxes support local government independence, it can also increase regional economic diversity, as ‘the rich get richer and the poor get poorer’;

• Although citizens may legally accept the tax, there is still widespread resentment in some lands for enforcing a policy, sometimes seen as a threat to domestic sanitation.

**Primary Rationale for Reform**

The four main principles for initiating property tax reform to improve fiscal performance, social equity, economic efficiency, or administrative cost effectiveness in all general reviews and direct application of these objectives to property tax reform in Karnataka state.

A fundamental failure of reform efforts may be a failure to clearly state the reason for the change, or to have previously unintended, contradictory motives. Low yields are the most common reason for the conversion of property taxes in the emerging economy, so consolidation of revenue is often the main reason for the conversion of property tax comparisons. Property tax reform is also neutral in financial matters if social, economic, or administrative considerations are more important, which is common in high-income countries. However, the reforms cannot be remedied to reduce tax rates in any country and survive. This is not the same as limiting the increase in tax revenue.

**Urban property tax reforms initiated in Indian cities:**

Since 1993 some states and cities in India have resorted to experiments in property tax reforms. Patna was the first city to undertake property tax reforms in 1993 by shifting toward an area-based valuation system. Around the same time, Andhra Pradesh also adopted a similar system, becoming the first State in the country to embrace the UAM. In 1999, Ahmedabad also undertook property tax reforms by adopting the essential elements of the Patna model. Bengaluru is considered to have the best property tax model in the country while Mumbai's model is ideal for replication in future. The initiatives undertaken by Hyderabad, Bengaluru and Mumbai are presented below.

**Hyderabad self-assessment scheme:**

The municipal corporation of Hyderabad introduced the UAM based property tax with a self-assessment scheme (SAS) in 1999–2000. The self-assessment system was chosen to prevent delays in formulating a new law. Properties were assigned unique property tax identification number and the taxpayers were given the option to determine their tax and file returns while revealing all property related details including plinth area. Resident Welfare Associations (RWAs) were closely involved, linking taxes to civic services area-wise. Some smart RWAs articulated three benchmark rents per sq. ft.—for high-rent, middle-rent and low-rent areas and proposed a minimum of 1 month of market rent as the benchmark for filing of tax returns. These views were articulated to other RWAs. These benchmarks were accepted by the municipal corporation to accept tax returns without going in for property-to-property

verification to bring all taxpayers to one level. The Hyderabad SAS was a resounding success. About 1,30,000 taxpayers filed self-assessment returns within 4 months of launching of the Scheme. A 123% increase in property tax was marked between 1999–2000 and 2001–2002 (70% in 1999–2000). The sources of the increase in yield have been a correction of historic inequities in the tax system, better coverage and record-keeping and computed-based decision support systems leading to better guidance to the tax administrators. The self-assessment of property tax scheme introduced in Hyderabad in 1999–2000 is continuing. However, property tax rates have not changed over the last 18 years. Between 2012–2013 and 2013–2014 the corporation has achieved remarkable success in property tax collection with a growth of 32% by strengthening enforcement and focusing on tax administration.

**Bengaluru self-assessment scheme:**

Bangalore has already faced two property tax reforms; the first was undertaken in 2000 within Bangalore City Corporation, and the second reform was combined with the formation of the BBMP by the State Government in 2007.However, the 2007 amalgamation has not yielded the expected gains; therefore, a new governance structure is expected.At the time of the 2007-merger, there was Annual Rental Value under the optional self-assessment system and the Capital Value System in place within the former BBMP area. Therefore, it was necessary to find a coherent property tax approach. In 2008, the Unit Area Value System was put in place by inserting a new section 108A into the Karnataka Municipal Corporation Act 1976. Since then, a uniform property tax is applied to the entire BBMP. The Annual Rateable Value (ARV) system was predominantly used before the formation of the BBMP. It shows some similarities to the Unit Area Value (UAV) system. The ARV system was based on the expected rent from the property; therefore, it would have reflected the location, quality of construction, usage, and age of the building without Rent Control. All the physical and usage features are typically reflected in the Annual Rental Value calculated per sq. ft. per month. The Unit Area Value system is based on the expected returns from the property depending on the location and usage of the property, and the age of the building. The new assessment method is called Unit Area Value, because it is based on the Unit measured per square foot per month, whereas the Area of the unit is reflected by a particular location (street name), which, in turn, determines the assessment Value by applying a property rate (value) to the unit based on the location. The Unit Area Values, so-called rates, are based on zones (area and street names), which were retained from the Rental Value system after the amalgamation to BBMP in order to incrementally change the property tax system. With the latest tax reform, self-assessment was introduced in order to bring all un-assessed properties into the

tax net. In this context, turning away from the tax authority toward taxpayer with regard to tax assessment has the huge advantage of switching the responsibility for property assessment. Self-assessment is mandatory, which includes so far unlawful properties, which now have to file the returns (physical and valuation-related information) to pay property tax. The new measures help to raise local own revenues, they improve horizontal equity among the taxpayers, and they increase the confidence that all taxpayers pay their due tax, which, in turn, results in higher tax compliance.

The property tax payable in Greater Bangalore is based on Unit Area Value with 20% tax rate applied. Beyond that, on the tax payable, another 15% Health Cess, 6% Library Cess, and 3% Beggary Cess are applied constituting the gross property tax payable.

The municipal corporation of Bengaluru provides a good example of property tax reforms, adopting the unit area value (UAV) method. It launched the optional SAS in 2000. The city was divided into six zones: A, B, C, D, E and F based on the guidance values notified by the Stamps and Registration Department of Karnataka Government. Residential use properties are classified into five categories and nonresidential use properties into 13 categories. For each zone, rental rates per square foot were determined linking buildings to location, type of construction, built-up area, use and age. Tax rates for rented buildings in Bengaluru were fixed at levels much lower than prevailing rates under the SAS. Owner-occupied buildings were given a concession of 50%. Two months deduction in annual rental value (ARV) was provided for repairs and so on. Further, the concession was given in accordance with the age of the building. The tax was levied at 20% of ARV for residential use and 25% for nonresidential use. Vacant land exceeding three times the built-up area is assessed at 30% of the rate fixed for the built-up area. To facilitate political acceptability, a cap on the property tax increase was set at 2.5 times the existing liability. The process was transparent and backed by political leaders. More than 60% of taxpayers filed their declarations within the prescribed 45-days period. Due to the SAS, property tax collection in Bengaluru increased by 33% during 2000–2001. Learning from the optional SAS-2000, Bengaluru has shifted to a mandatory scheme by amending the Karnataka Municipal Corporations Act 1976 to provide for self-assessment based on UAV. SAS-2008 has shifted to the concept of UAV from ARV in SAS2000. Filing of annual property tax returns in Bengaluru is now mandatory. Up to 10% of the returns filed are required to be verified randomly. The municipal corporation has supplied a handbook to taxpayers at a nominal cost, explaining how self-assessment property tax can be calculated. An online tax calculator is also made available. Then, 360 help centers were organized to propagate the features of SAS to citizens and clarify their doubts. Now

property tax can be paid online, at computerized kiosks in "Bangalore One" centers, municipal offices or banks. Credit card payments facilities are also available with no user charges to citizens. Property-owners who make payments in full before April 30 can avail a rebate of 5%. Penalty at 2% per month is levied on defaulters after 60 days from the date property tax is due—April for first half-year and October for second half-year. It is mandatory for all properties, including unlawful properties and those in unauthorized layouts to pay property tax without any assurance of regularization. Over a 3-year-cycle, the value increase must be at least 15%, resulting in steadily increasing property tax collection. Bengaluru adopted GIS-enabled database for property tax on a city-wide scale, identifying 1.7 million properties and assigning them unique numbers for Property Identification and became the first city in India to do so. Due to SAS-2008, property tax collection in Greater Bengaluru Municipal Corporation increased by 39% between 2009–2010 and 2010–2011. The tempo of property tax growth in the city is continuing. It has reportedly reached about Rs.1,800crores in 2015–2016.

**Mumbai capital value-based property tax:**

The municipal corporation of Greater Mumbai has shifted from the ARV-based property tax to a capital value-based system in 2010. Under the new scheme, the market value of the property is determined based on the stamp duty ready reckoner, revised by the Government of Maharashtra every year. The market value is then multiplied with the carpet area of the property (land area in the case of open land) and weight factors notified by the corporation, including nature and type of construction, age of the building, floor characteristics and use of the property. This gives the property's capital value, which multiplied with the property tax rate notified by the city council, determines the property tax payable. Property tax rates are notified by the municipal corporation of Greater Mumbai from time to time under various components: general tax (including fire tax), street tax, municipal education cess, water tax, water benefit tax, sewerage tax, sewerage benefit tax and tree cess. The combined tax rates for various user categories ranged from 0.316% to 2.296% in 2013. However, the capital value-based system in Mumbai is yet to be firmly established.

**Impact of Tax reforms on Municipal tax methods**

Despite the reforms attempted by the Indian cities, the results are not as expected. The reasons for the sub-optimal results, are rooted in the very form and nature of reforms attempted in the Indian Cities. Many of the Indian cities are still following the rental value method, which limits the scope of generating higher revenues from property taxes. Under the rent control regime, property taxes based on the rental value method are underestimated

figures. There can be a significant difference between market value and rental value; especially when properties are not put to "highest and best" use. Vacant lands cannot be taxed under this method because they generate no rent. The UAM is also laced with several disadvantages. To begin with, the size of a property is not an appropriate measure of the benefits drawn from the provision of civic services. A better proxy for the benefits drawn is the value of the property. The area-based method is criticized for being unfair to low-income groups. The reason is that in a specific zone there are high-value as well as low value neighborhoods and properties of the same size have to pay the same amount. Average household incomes are higher in high value neighborhoods than in low-value neighborhoods. Thus, it is considered regressive. Older houses with large floor area may be in a bad shape, but such structures are also subjected to relatively high taxes. Due to certain changes like a new transit facility or a new school, the value of a zone increases. However, such increases do not reflect in higher property tax revenue due to the lack of proper revision of property values. Over a while, it results in an iniquitous assessment system. Allocation of shared facilities like lobby, common entrances and exits, halls etc. among the owners is yet another problem. The UAV method may be critically evaluated. The method does not seem to be yielding desirable results in the case of nonresidential properties. Although unit value may be easier to administer for single-family residential properties, it is difficult to use for multi-residential rental, residential condominium, commercial and industrial properties (Bird & Slack, 2004). Such properties are highly heterogeneous and the method of "averaging" inherent in the UAM may be leading to the subsidization of high-end commercial properties and penalization of those at the lower ends. Larger and more prosperous cities are not necessarily adopting higher unit area rates. Commercial properties in wealthier cities are not necessarily paying property tax at higher rates than less well-off cities.

UAM rates are not revised from time to time. This has led to a lack of buoyancy in the collection of property tax in all cities. Unit area rates have not kept pace with the rise in land and property values due to urbanization and economic growth. This means that Indian cities are not able to capture these gains and are foregoing important revenues. There is no built-in provision under the UAM to index property tax to inflation. Even the self-assessment method is not free from drawbacks. Compliance and litigation are two issues associated with self-assessment. If all the owners do not comply then it is difficult to determine the number of taxpayers or taxable properties. Generally, random sampling is adopted to verify if the self-assessment forms submitted reflect the tax liability accurately. For example, in Bengaluru, up to 10% of the returns filed are verified randomly. There may be cases of underestimation of

tax liability in the absence of property inspection by qualified personnel. It is understood that without a reliable verification technique, it is not possible to encourage people to tax themselves. Inaccurate assessments and underestimation can result in significant loss to municipalities by eroding the tax base.

Some of the lessons from property tax reforms carried out by cities include the following:

- The tax system must be simple and easily understandable to the public;
- Fixation of tax should not be arbitrary; the tax rate must be linked to the tax base by a formula pre-determined by law and not subject to the discretion of any bureaucrat;
- The tax rate should be reasonably low so that compliance would be high;
- The tax system should not only be fair, but also be perceived to be fair by the taxpayers;
- The system of levy and collection should be transparent and not prone to manipulation for graft or corruption;
- The taxpayers should be involved in the decisions regarding tax reforms; tax education is critically important for the success of property tax reforms;
- The taxpayers need to be made aware that what they pay translate into services; visibility in the provision of services in the tax-paying areas enhances the willingness to pay; and
- Tax reforms should be well-timed and not be unnecessarily linked to time consuming processes as opportune times do not last long.

## SUMMARY,MAJOR FINDINGS, AND CONCLUSIONS

### Summary

In India, the government administration is of three forms, Central, states and local governments. In a federal setup the central government is superior to all other units. Local bodies form the third layer of the federal government. Local self-government in India has now become an integral part of the national administrative machinery and plays an important role in economic planning. Both planning and its implementation can become more realistic and effective with the participation of the people at local levels. Local government plays an important role for the development of local citizens. Moreover, local self-governments lay the foundation for sensible and responsible training to the citizens in the matters of political, social and economic rights and obligations. Local government is the last preserve of people near direct participation in their civic affairs management. Local government is described as that under which the people of the locality possess a certain responsibility and choice in the administration of public affairs and in the raising of the

required finance to meet their expenses. Local self-government can work smoothly only when the resources at their disposal are adequate and they are effectively utilized. Effective utilization of funds is fundamental to bringing about the desired improvement in civic life.

The existence of a wide gap between the income and expenditure of Municipal bodies has led to a serious thinking on the part of the administrators' policy makers and academic thinkers about the management of finances of these local institutions. The Problem of huge budgetary gap has been further made more complex by the ever-growing control and regulation of the finances of these bodies by the state government resulting in very little scope for the financial autonomy of the Municipal Corporations. The responsibilities of the Municipal Corporation have been expanding due to the fast-growing urbanization and the ideal of social welfare as a state policy. The income position of these bodies is almost stagnant due to inelasticity of their taxes, which are limited in their content and coverage while the expenditure position of the Municipal Corporations is becoming unmanageable due to the expanding demand for the civic amenities.

**Major Findings and Conclusions:**

The importance of property tax for municipalities manifests itself in the form of huge revenue potential. It represents the autonomy and strength of local "self-government" and participatory democracy. It has tremendous potential to raise revenues for city services and development. However, the tax has been grossly neglected by cities in India for decades. Property tax has beensubjected to under-exploitation due to systemic problems as well as inefficiencies in municipal tax administration. Property tax collection in India has not kept pace with the demands of urbanization and economic growth.

This study suggests that a comprehensive approach to property tax reforms must address systemic design as well as collection-related issues. A system without collection is meaningless and collection is not sustainable without a proper system in place. The systemic reforms require a robust regulatory framework which covers the various dimensions of the tax base, tax rate, tax liability, property valuation, revaluation, exemptions, billing, collection and dispute resolution.

Professionalization of the tax administration with expertise, technology, tools, GIS mapping and MISs is also required. Seamless integration of multiple databases can improve record-keeping and reduce tax evasion. E-collection of property tax: online and through computerized kiosks, service centers or banks, as in Hyderabad and Bengaluru, can save a lot of time and effort. Improved collection mechanism is the key to a well-functioning property tax system.

At present, property tax is the only major municipal tax and its reform is mandatory to pull Indian cities out of the "rich city-poor city government" phenomenon. Property tax reforms will bring with it revenues to undertake planned urban infrastructure development projects,apart from meeting the costs of collective civic services. Cities have agglomeration economies and this leads to a substantial increase in land and property values, rents, number of commercial properties etc. If property tax is designed properly and collected efficiently then it can prove to be a revenue-productive and buoyant tax to finance India's urban transformation.

- There has been a tremendous increase in the responsibilities of Municipal bodies as a result of two factors viz.,
  (i) rapid increase in urbanization and
  (ii) adoption of Welfare state as national policy
- Municipal Corporations have two types of functions viz.,
  (i) Obligatory and
  (ii) Discretionary.
  Obligatory functions of Municipal Corporations include water supply, electricity, road, transport service, lightning, watering and cleaning of public streets, establishment and maintenance of hospitals and primary health centers, control and regulation of eating places and eatables and registration of births and deaths. Discretionary functions include construction and maintenance of public parks, gardens, libraries, theaters, stadium, provision of public housing, relief to disabled and destitute, detention and control over stray animals, registration of marriages and organisation of fairs exhibitions etc.
- The usual revenue sources of municipal bodies are broadly divided into
  (i) Tax Revenue
  (ii) non-Tax Revenue
  (iii) revenue from remunerative enterprises maintained by the corporation and
  (iv) grants-in-aid
- Tax source of revenue of Municipal corporation are
  (i) Property tax
  (ii) Water Tax
  (iii) Entertainment Tax
  (iv) profession Tax and
  (v) Tax on advertisement etc.

- The non-Tax Revenue source are
  (i) fees relating to buildings
  (ii) fees under communicating system
  (iii) license fees for dangerous traders
- The revenue from remunerative enterprises includes enterprises like poultries, cinema theatres and commercial complex etc.
- Various types of grants from the State and Central Governments are given to the urban local bodies. This is an important source of finance for these bodies.
- Municipal finances have their own distinct features and significance. They pertain to performance of essential local activities and services. Their performances involve immediate local attention, direction, control and supervision.
- The budget of the Municipal Corporation is prepared at the beginning of the fiscal year and a copy of the statement of the estimated receipts and expenditure of the year is submitted to the state government. The state government can modify or ask the local bodies to modify or revise the budget within thirty days of the receipt of the budget which shall be deemed to be sanctioned budget of the municipal corporation. This way the state government exercises control over the finances of the municipal bodies.
- The state government exercises control over the finances of the municipal bodies through
  (i) sanctioning of local loans and associated devices on per capita expenditure and through cost control and
  (ii) restricting the level of grant-in-aid to urban local bodies i.e. control over revenue expenditure.
- Accounting provides the day-to-day financial transactions, the receipt of revenue and the payment of expenses. The Municipal Accounts adopt the cash basis though a widely recognized practice is to have a combination of cash basis and accrual basis of accounting for Municipalities. Under this practice revenue is recorded only when cash is received while expenses and related liabilities are recorded when incurred.
- Auditing of municipal accounts is carried out by Local Fund Audit Department. Accounting and auditing function as custodians of the public money. Audit is tool of financial control. Audit of Municipal bodies is either pre or post audit. Pre audit is considered to be more effective instrument of financial control while post audit is post mortem of the expenditure, which has already been incurred.

- The dwindling resources of the Municipal Corporation is a matter of concern for these bodies. The expanding role of the Corporation is providing civic amenities and facilities is not matched by proportionate increase in their revenue resources. The Tax base is shrinking and is inelastic since the state government has taken over most of the elastic sources of revenue. The abolition of Octroi has further eroded the revenue resources of the municipal bodies.
- The problem of incompetent personnel is affecting the municipal administration. Good quality and competent personnel are not attracted to these local bodies due to meagre promotional opportunities in these institutions. The morale of the existing personnel is low.
- The problem of the Government control over the municipal bodies is too severe curbing the initiative of the local administration. The legal provisions governing the Municipal bodies have given tight control over them by the state government. The state government has complete control over their finances and it can dissolve and supersede these bodies at will.
- The problem of fast-growing urbanization is creating difficulties for the management of the civic amenities for the urban population. The problem of the slum development due to urbanization in the wake of fast-growing industrial activities is another severe challenge to civic administration.
- The Municipal administration is faced with problems of corruption, political influence, factionalism, communalism etc.
- All the six largest Municipal Corporations have introduced self-assessment of property tax.
- Online and mobile based payments, payment facilities at specific bank branches and citizen facility centers, e-mailing tax bills, online tax calculators and electronic display of tax bills are simple measures that improve compliance and encourage transparency.
- 'Early Bird Schemes' in which discounts are available on timely payment of property tax bills have been utilized by some of these Municipal Corporations to improve collection rates.
- Effective public information campaigns help widen tax base and are also especially necessary during revision in rates or switch to a new valuation system.
- Kolkata's move to the unit area value system was marred by complicated assessment methodology and ambiguous assessment forms. Strict enforcement measures are necessary to improve collections.

- Bengaluru has initiated a Total Station Survey i.e., a survey using total station machines, to identify the top hundred commercial and residential enclaves in every zone and impose stringent measures on those declaring lower tax.
- It has also set up a Revenue Vigilance Cell and a High Value Properties Tax Recovery Cell to improve tax revenues. Ahmedabad sealed over 5473 properties including some public sector units in 2019 for defaulting on their property tax payments. This led to an uptick in property tax revenues for the fiscal year 2018-19.

**SUGGESTIONS**

**(i) Revenue**

- Tax revenue constitutes an important source of income. Among the revenue side property tax is the most important items of tax collection. On an average more than 50 per cent tax revenue is contributed by way of property tax. So the property tax has been revised regularly. Property tax assessment should be strengthened scientifically and systematically.
- Rebate should be allowed for payment in time and penalty should be imposed for delayed payment.
- Shortage of staff on clerical and collection side, shifting of staff for tax-revision purpose and election activities have adversely affected the collection of tax revenue. So, strict measure should be taken to recover the arrears. The tax collection machinery should be tightened and the executive officers should be made responsible for proper collection. Persons who have special knowledge and training in the valuation of properties must be employed for the determination of the annual rental value of private buildings.
- Entertainment tax is a local tax in many countries of the world. It is suggested that state government should transfer entertainment tax or a substantial share of it not less than 90 per cent to the municipal corporation.
- In order to perform its functions very effectively and successfully Municipal Corporations should act quickly to expand their non-tax revenue. It should undertake public utility services such as the distribution of gas or electricity and running of transport organization.
- The Municipal Corporation should be free from political interference. The budget prepared by the Municipal Corporations must be strong and take into consideration availability of the resources that are urgently needed from the residence. It must

follow strict rules to collect the tax and non-tax revenue every year without much arrears.

- The Municipal Corporation should establish effective relationship with the public.

**(ii) Expenditure**

- The cost of administration had increased manifold during the year. There has been leakage of large amounts of revenue to negligence and malpractices by the compensation of employers. Hence, there is greater need for increased supervisory control.
- The Municipal Corporations should frame a five-year development plan so that long – deferred projects can be effectively implemented within a specific period.
- The Municipal Corporation is extending different kinds of welfare measures through different departments but many of these programmes do not reach the intended beneficiaries. The illiterates in the urban areas are ignorant of these welfare programmes. The corporation should act as the information centre for activities so that the programmes should reach the intended beneficiaries.
- Some kind of expenditure control measures should also be introduced to improve the finances of Municipal Corporations. There is an urgent need to improve the quality and contents of expenditure programmes of the corporations.
- Environment is a broader subject. In order to bring effective pollution control, the corporations should take up their share of responsibility in minimizing the pollution efforts of solid waste, water resignation and savage.

**Conclusion:**

- The rapidly growing metropolitan cities of India are the engines of economic growth for the country. In the coming years, these cities will expand geographically and attract more migrants in search of employment opportunities.
- Municipal Corporations are responsible for the infrastructure and public service delivery in these cities; they need better governance as well as stronger finances to handle the demands of the rising population.
- Tax reform strategy depends to a great extent on the pre-conditions; but certain principles such as the close involvement of the tax paper, tax-service linkage, incentives for filing of tax returns, disincentives for non-filing, tax education, etc., are important in the designing of successful reforms.

- Along with the fair valuation of property, periodic and regular re-assessment of the property tax base is critical to bring assessed values in line with market realities.
- In municipal Acts of many states, it is recommended to carry out an assessment of properties once in every five or four years. These reforms have typically focused on improving the administration of the tax, and in some cases accompanied by changes in valuation of the tax base.
- Correction of inequities in the tax system can be an important source of enhanced mobilisation of property tax revenues in most cities. Keeping tax rates low and emphasising on compliance led to significant increases in property tax collection in Hyderabad.
- Tax education and organised publicity campaigns to address the psychology of tax-payer are often more important than economic factors such as tax rate and tax base in realising the potential of property tax; people must perceive the tax system to be fair and appreciate the linkage between tax and service provision.
- Direct involvement of tax-payers in the provision of civic services is a must for better tax compliance
- Tax reforms may need to be pursued in an incremental manner. Elaborate and time-consuming design may lead to the bouncing back of effort to clean a tax system.
- One of the improvement objectives of the property tax reform should be to reduce the extent of under valuation by employing better techniques of assessment, which can yield greater accuracy and precision.

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